

PHILIPS

Broadcast Flag Technology Licensing Safeguards

May 28, 2004

Overview

- DTCP, CPRM & HDCP each contain specific license terms that violate the Broadcast Flag Order's requirement that licensing be on a "reasonable and non-discriminatory" basis
- These license terms threaten competition
- The FCC should condition approval of these technologies on reform of these licenses

What Philips is NOT seeking with regard to DTCP, CPRM or HDCP

- Rejection by the FCC
- Delay
- Wholesale revision
- Third-party review of patents
 - Patent lists need not be exhaustive

What Philips IS seeking

- Conditioning approval of the DTCP, CPRM and HDCP technologies upon reform of licenses to comply with the FCC's "reasonable and non-discriminatory" licensing requirement
 - Specific changes focused primarily on **3 provisions** (among hundreds):
 - Non-Asserts
 - Approval of Downstream Technologies
 - Change Management
- FCC articulation of limitations on scope of its approvals

Special Need for FCC Review of Broadcast Flag License Terms

- Manufacturers must license the approved technologies to comply with a gov't regulation
 - FCC already has intervened in the market
- Broadcast Flag Order greatly expands the market for digital recording protection technologies
- Reasonable and non-discriminatory licensing is essential to effectuate FCC's goal that no industry segment control decisions

The FCC Cannot Rely on Market Forces Alone To Create A Competitive Market

- In the case of DTCP, HDCP and CPRM, at least one or more of the following apply:
 - Dominance due to head-start, first-mover advantage, combined with “network effects”
 - Manufacturers cannot avoid licensing DTCP and HDCP (or CPRM for DVD-R, DVD-RW and DVD-RAM formats) to make Broadcast Flag-compliant products
 - Group of competitors with market power joining to license other direct competitors

DTCP

Hitachi, Intel, Matsushita, Sony, Toshiba

- Only available link protection technology proposed to FCC that permits recording or the carriage of compressed content
 - Any manufacturer of...
 - DTV receivers
 - PVRs
 - DVD players/recorders
 - Set-top boxes
- ...will need to license DTCP

HDCP

Intel

- Only available protection technology proposed to FCC for uncompressed video to displays
- Any manufacturer of...
 - DTV receivers
 - PVRs
 - DVD players/recorders
 - Set-top boxes...will need to license HDCP

CPRM

IBM, Intel, Matsushita, Toshiba

- Only available recording technology for the DVD-R, DVD-RW and DVD-RAM format proposed to FCC
- Any manufacturer of DVD-R, DVD-RW and DVD-RAM players/recorders will need to license CPRM

Non-Assert Provisions

Non-Assert Provisions Are Neither Reasonable Nor Non-Discriminatory

- Licensees forced to forfeit the value of their IP to protect the IP value of others
- Discriminates against licensees with IP vs. those without IP
- Non-Asserts subject to expansion resulting from changes to the Specifications

Non-Assert Provisions Are Neither Reasonable Nor Non-Discriminatory

- Inclusion of Non-Assert in DTCP and CPRM licenses is highly irregular and unjustified
 - Licensors admit that patent pools are not involved here
 - Absence of a legitimate patent pool eliminates pro-competitive benefits of joint action
 - No possible justification for Non-Asserts

Non-Assert Provisions Discourage R&D Investment

- Royalty payments on patents promote innovation
 - Just as the ability of content owners to collect royalties on their IP promotes investment in new content, the ability of patent owners to collect royalties for their IP promotes technological innovation and competition
- Non-Asserts discourage investment in R&D
 - Research projects such as localization may be abandoned if investments risk being stranded by Non-Asserts that preclude IP royalties
 - Antithetical to content protection goals!

Meritless Defenses of Non-Asserts

- Claim: *Number of signatories proves acceptability*
 - Proves only market power and head-start, not RAND
- Claim: *Too many existing licensees to change*
 - Agreement can offer licensees a choice of: (a) participating in the reciprocal Non-Asserts between the current licensees; or (b) participating on RAND basis.
 - Microsoft has removed its Non-Assert for new agreements

Meritless Defenses of Non-Asserts

- Claim: *Non-Asserts are essential to cost-recovery-based licensing structure*
 - Approach amounts to forced subsidization by licensees with IP
 - Licensors provide no evidence that fees are limited to cost recovery

Non-Asserts Rejected In Other Contexts

- Expressly rejected in DFAST license
- Abandoned by Microsoft in wake of antitrust litigation

Extra-Regulatory Veto
of FCC-Approved
Downstream Technologies

Licensors Veto of FCC-Approved Downstream Technologies Is Neither Reasonable Nor Non-Discriminatory

- No rational basis for withholding approval of any downstream protection technology if the FCC has approved it
- Affords direct control over consumer use of competing technologies
 - Grants industry segment control over technology approval
 - Creates an entry hurdle for competing technologies

Meritless Defenses of Downstream Technology Veto

- Claim: *FCC may approve ineffective downstream technologies*
 - Presupposes failure of FCC review process
 - Studios do not oppose alternative licensing model that accept all FCC- approved technologies
 - Model contained in Vidi, SmartRight and WindowsMedia

Meritless Defenses of Downstream Technology Veto

- Claim: *Automatic approval creates technical problems*
 - None of the 5C objections prevents DTCP or CPRM from handing off to any other FCC-approved technology. Issue is purely licensing, not technical

Change Management Provisions

Change Management Procedures Neither Reasonable Nor Non- Discriminatory

- Changes provisions are not narrow
 - Specification may be expanded for use with new transports (e.g., DTCP-IP)
 - Such changes may involve a completely new system or technology
 - Open-ended changes to Compliance Rules where “necessary to ensure and maintain content protection” could impose significant new costs on manufacturers
- No dispute resolution procedures for licensees
- Licensors offer no defense to process concerns

Anticompetitive Effects of Changes Provisions

- Materially affects direct competitors' product decisions
- Exacerbates problem of lead time-to-market advantage
- Potentially expands scope of Non-Assert
 - Increasing number and lost value of patents affected

Model Approaches to Change Management Exist

- The DFAST, Vidi, and SmartRight licenses all take a reasonable approach to change management
 - Clear and narrow limitations on scope
 - Reasonable notice
 - Meaningful opportunity for comment and negotiation
 - Impartial disputes resolution
 - Reasonable implementation period

Summary: Specific Changes Sought

- Licensees given a choice between RAND and reciprocal Non-Assert
- Acceptance of FCC approval of downstream technology as binding
- Change process for Specification and Compliance and Robustness Rules providing:
 - reasonable notice
 - opportunity for comment
 - meaningful dispute resolution process
 - reasonable implementation time